No. 508

In the Supreme Court of the United States

OCTOBER TERM, 1952

UNITED STATES OF AMERICA, PETITIONER

v.

INTERNATIONAL BUILDING COMPANY, A CORPORATION

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

REPLY BRIEF FOR THE UNITED STATES

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Respondent's brief contains arguments and authorities which relate, for the most part, to issues as to which there is no dispute in this case. For that reason it may be helpful to restate what the Government's position is, and what it is not:

1. Concededly, a decision of the Tax Court entered upon a stipulation of the parties that there is no deficiency, or that there is a deficiency or overpayment of x dollars, is conclusive in all respects as to the liability for the tax year to which it relates. Such a decision is *res judicata*, in the fullest sense, in any subsequent proceeding involving the same taxpayer, the same claim, and the

same tax year.[1] Neither the taxpayer nor the Commissioner can thereafter, on any ground other than those traditionally available to overcome *res judicata* (*e.g.*, fraud, duress, lack of jurisdiction), seek to reduce or increase the taxpayer's liability for the claim and year concerned. *Continental Petroleum Co.* v. *United States*, 87 F. 2d 91 (C.A. 10); *Backus* v. *United States*, 59 F. 2d 242 (C. Cls.); *American Woolen Co.* v. *United States*, 18 F. Supp. 783, 788-789 (C. Cls.); *Lehigh Valley Trust Co.* v. *United States*, 34 F. Supp. 839 (E.D. Pa.); *Almours Securities, Inc.*, 35 B.T.A. 61, 68-69; cf. Sec. 322(c), Internal Revenue Code (26 U.S.C. 1946 ed. 322(c)).

2. As to tax liability for succeeding years, the effect of a Tax Court decision depends on the application of the doctrine of collateral estoppel. "Income taxes are levied on an annual basis. Each year is the origin of a new liability and of a separate cause of action. Thus if a claim of liability or non-liability relating to a particular tax year is litigated, a judgment on the merits is *res judicata* as to any subsequent proceeding involving the same claim and the same tax year. But if the later proceeding is concerned with a similar or unlike claim relating to a different tax year, the prior judgment acts as a collateral estoppel only as to those matters in the second proceeding which were actually pre-

[1] Where the later proceeding involves the same year but a different claim, not presented to or decided by the Tax Court, its decision is, of course, not *res judicata* in any sense. *United States* v. *Erie Forge Co.*, 191 F. 2d 627 (C.A. 3).

sented and determined in the first suit." *Commissioner* v. *Sunnen*, 333 U. S. 591, 598; *Tait* v. *Western Md. Ry. Co.*, 289 U. S. 620, 623-625.

3. Concededly, where the Tax Court has decided controverted issues of fact, or where the parties have stipulated facts which the Tax Court has accepted, such facts are conclusive in proceedings between the parties for later years, subject to the qualification that "the legal matter raised in the second proceeding must involve the same set of events or documents and the same bundle of legal principles that contributed to the rendering of the first judgment." *Commissioner* v. *Sunnen, supra*, pp. 601-602; *Tait* v. *Western Md. Ry. Co., supra*, pp. 625-626; *Commissioner* v. *Texas-Empire Pipe Line Co.*, 176 F. 2d 523 (C.A. 10); *Arthur C. James*, 31 B.T.A. 712, 719; cf. *Pelham Hall Co.* v. *Hassett*, 147 F. 2d 63 (C.A. 1); *Blaffer* v. *Commissioner*, 134 F. 2d 389, 390 (C.A. 5); *Stanback* v. *Robertson*, 183 F. 2d 889, 894 (C.A. 4); *Sam Schnitzer*, 13 T.C. 43, 55-56, affirmed 183 F. 2d 70 (C.A. 9),[2]

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[2] Thus, in the *Pelham Hall* case, *supra*, the Board of Tax Appeals, in a sharply contested proceeding relating to the year 1931, had affirmed the Commissioner's determination that taxpayer's depreciation base on a certain building was $362,700. In a later proceeding involving the year 1936, the taxpayer contended that the transaction in which it had acquired the building was a tax-free reorganization and that it therefore was entitled to take over the base used by its predecessor, *i.e.*, $806,000. Although the Commissioner argued that the $362,700 base was made *res judicata* by the decision for the year 1931, the Court of Appeals rejected his plea. It pointed out that in the earlier proceedings no claim was made that the acquisition was part of a tax-free reorganization, and that even though the Board had expressly stated in its opinion that "The new corporation started upon a new basis and its depreciation is meas-

4. Where, however, as in this case, the parties file a stipulation in the Tax Court which recites that the parties have agreed that there is no deficiency due from the taxpayer for the year in controversy, or that there is a deficiency or overpayment of *x* dollars, and no other facts are stipulated, the Tax Court treats such a stipulation as an effective disposition of the case, and enters a formal order carrying out the agreement of the parties without any examination into the merits of any issues of fact or law which might be involved. No hearing is held, no evidence received, no briefs filed, and no arguments made in connection with the entry of orders based on such stipulations.

In the Appendix to this brief (p. 10, *infra*) is printed a letter of Victor S. Mersch, Esq., Clerk

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urable accordingly", this statement meant only that the Board was accepting the issue as tendered in the petition and was "making the same assumption which had been made by the Commissioner and the taxpayer, that the refinancing transaction was not a tax-free reorganization." (147 F. 2d at 66.)

The court noted that when the taxpayer filed its petition for review with the Board for the year 1931, the "indications then were that the transaction would not be held to be a tax-free reorganization," but that since that time it had become clear from intervening decisions of this Court that the transaction would be so regarded. It concluded that the taxpayer should not, for years after 1931, be forever barred from using the depreciation base of its transferor, which it would otherwise be entitled to do, because of a collateral estoppel created by the 1931 decision. The court held that in the 1931 proceedings "the Board had before it no controverted issue as to whether the transaction was a tax-free reorganization; that no such question was 'actually litigated and determined' by the Board within the meaning of the rule as laid down in the *Cromwell* case." Judge Magruder's opinion for the court stated (147 F. 2d at 67):

> It would be possible to play with words by asserting that the issue presented to the Board was whether the Com-

of the Tax Court, dated March 25, 1953, in which he describes the practice of that court with respect to decisions based upon such stipulations.[3] Mr. Mersch states:

> After a stipulation of deficiency has been received and docketed, the Clerk of the Court or one of his Deputies examines the pleadings of the case and verifies that the stipulation will determine the tax liabilities involved in the litigation and effect a complete disposition of the case. Thereupon he prepares from the stipulation an appropriate form of decision to be entered by the Court.
>
> It is not the practice of the Court itself otherwise to check the pleadings before the decision is signed and entered. In fact, in many of these cases, the decision is entered in

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missioner was in error in reducing the taxpayer's basis for depreciation to $362,700; that the Board's decision upheld the Commissioner's determination; and that the taxpayer cannot escape the binding effect of this decision in litigation involving the same issue for a succeeding tax year by producing a new argument or new evidence in support of the proposition previously decided against it. See *Tait* v. *Western Maryland R. Co.*, 1933, 4 Cir., 62 F. 2d 933, 935. The matter should be put this way only if the policy behind the doctrine of collateral estoppel by judgment is deemed to be so strong that the courts should be astute to give the doctrine the widest possible application. We believe, on the contrary, that particularly as regards questions of law in tax cases, collateral estoppel by judgment should be rather narrowly applied. To minimize the recurring hardship to the taxpayer or prejudice to the revenue (as the case may be), with respect to the taxes for all succeeding tax years, neither the taxpayer nor the government should be precluded from raising a relevant point of law unless it appears beyond doubt that the precise point was actually contested and decided (not merely assumed) in the prior litigation.

[3] This letter has been filed with the Clerk of this Court.

the name of the Chief Judge by action of the Clerk or the Chief Deputy Clerk.

Apart from the decision below in this case, it has been consistently recognized that such a decision of the Tax Court, although conclusive as to the tax claim and year to which it relates, can not form the basis of a collateral estoppel for future years as to any issue involved, because no determination on the merits is made. (See cases cited in our main brief, pp 21-22.) A decision based on a stipulation of a specified deficiency or overpayment, and "not predicated upon stipulated facts, or upon findings of fact, or upon a determination on the merits, but merely to carry out a compromise agreement of the parties, fails to constitute an effective judicial determination of any litigated right" and "will not support a plea of estoppel." *Trapp* v. *United States*, 177 F. 2d 1, 5 (C.A. 10). "Where the entire controversy is disposed of by the Board on stipulation and without any consideration, there has been no adjudication." Griswold, *Res Judicata in Federal Tax Cases*, 46 Yale L. J. 1320, 1338.

The Tax Court, which is the best judge of the nature and effect of its own determinations, has expressly marked the difference between decisions based upon a stipulation of facts and those based upon a stipulation of deficiency or overpayment, without reference to any underlying issues of fact or law. In the leading case of *Margaret A. C. Riter*, 3 T. C. 301, reviewed by the entire court and decided February 18, 1944, Judge Murdock (who

signed the orders in the present case on October 17, 1944—R. 52, 54) wrote (3 T.C. 305):

> We have heretofore held that a judgment based upon a stipulation such as was filed in complete settlement of the 1936 case (as opposed to a stipulation of facts upon which a tribunal has based its independent judgment, see *Arthur Curtiss James*, 31 B. T. A. 712) is not a decision on the merits which will support a plea of the kind here made, raised as it is in a proceeding involving a different cause of action. See *Almours Securities, Inc.*, 35 B. T. A. 61, 69; *Volunteer State Life Ins. Co.*, 35 B. T. A. 491, 494; * * *.

In *Almours Securities, Inc.*, 35 B. T. A. 61, 69, affirmed, 91 F. 2d 427 (C.A. 5), certiorari denied, 302 U. S. 765, a no-deficiency stipulation and order thereon for the years 1927, 1928, and 1929 had been entered, and the taxpayer contended that the order created an estoppel on the merits for the years 1931 and 1932. The Commissioner admitted that the prior decision was conclusive, but only as to the years to which it related. The Board held that no estoppel was created as to the later years, since "neither the law nor the facts of the case were judicially ascertained. When the petitioner [taxpayer] and the respondent submitted the stipulation [in the prior proceedings], the Board was not advised as to the reason for the stipulation. For aught the Board knew there had been an error on the part of the respondent [Commissioner] in the determination of the deficiencies * * *".

Similarly, in *Volunteer State Life Insurance Co.*, 35 B. T. A. 491, 494-495, a Board order entered pursuant to a stipulation of the parties that there was an overpayment of tax for the year 1928 in a specified amount was held to be "a disposition of the suit by the parties and not by the Board * * *. It was not a judicial rendition on the merits and can not be the basis of a claim of res judicata in the present proceeding [involving the years 1929 and 1930]."

Respondent argues (Br. 13-14) that a distinction should be drawn between "compromise stipulations" and "confession stipulations". The former, respondent concedes, create no estoppel because "In the compromise settlement cases, nothing is decided or determined because the compromise is based upon neither a fact alleged in a taxpayer's petition, or the Commissioner's answer. A compromise is a settlement by mutual concessions. In the instant case there were no mutual concessions. There was a cold bald admission and confession which settled the entire controversy on the sole issue in the case."

This argument is not supported by the cases, which neither mention nor substantiate any such distinction. The Tax Court has applied the rule of the *Riter* case to all orders based on stipulations disposing of an entire controversy, without stopping to inquire whether the concessions were mutual or entirely unilateral. (See cases cited in our main brief, p. 21.) In any event, respondent's argument overlooks the central fact upon which the *Riter*

rule rests, namely, that orders entered on such stipulations are in no sense determinations on the merits of any issue involved. They serve merely to dispose of the case in accordance with the agreement of the parties, entered into for undisclosed reasons which may have nothing whatsoever to do with the merits. Both the Commissioner and taxpayer may prefer that the controversy be postponed to another day or to another forum. The amount involved for the particular year may be too small; the burden and expense of investigation and trial may, at the time, be too great; these and other reasons may commend themselves to both the Commissioner and the taxpayer as justifying settlement for the particular year without thereby waiving any rights for future years. And the procedure followed by the Tax Court in entering orders based on such settlements, is consistent with its recognition that these orders are not decisions on the merits and create no estoppel for future years.

Respectfully submitted.

ROBERT L. STERN,
Acting Solicitor General.

H. BRIAN HOLLAND,
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ELLIS N. SLACK,
LEE A. JACKSON,
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Special Assistants to the Attorney General.

APRIL 1953.

APPENDIX

THE TAX COURT OF THE UNITED STATES

Washington 25, D. C.

March 25, 1953

Honorable Robert L. Stern
Acting Solicitor General
Department of Justice
Washington, D. C.

Dear Mr. Stern:

In response to request from your office, you are advised that the practice of this Court with respect to decisions based upon stipulations of the parties or their attorneys as to the amount of deficiency or overpayment in any given case is as follows.

After a stipulation of deficiency has been received and docketed, the Clerk of the Court or one of his Deputies examines the pleadings of the case and verifies that the stipulation will determine the tax liabilities involved in the litigation and effect a complete disposition of the case. Thereupon he prepares from the stipulation an appropriate form of decision to be entered by the Court.

It is not the practice of the Court itself otherwise to check the pleadings before the decision is signed and entered. In fact, in many of these cases, the decision is entered in the name of the Chief Judge by action of the Clerk or the Chief Deputy Clerk.

Trusting this is the information desired, I am,

Very respectfully,

(S.) VICTOR S. MERSCH,
Clerk.

VSM/egh

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